CBA | CONSUMER BANKERS ASSOCIATION

January 30, 2004

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
Via e-mail to: regs.comments@federalreserve.gov

Attn: Docket Number R-1167 (Truth in Lending)
Docket Number R-1168 (Equal Credit Opportunity)
Docket Number R-1169 (Electronic Fund Transfers)
Docket Number R-1170 (Consumer Leasing)
Docket Number R-1171 (Truth in Savings)

Re: Proposed Changes to Regulations Z, B, E, M and DD

Dear Ms. Johnson:

This letter is submitted on behalf of the Consumer Bankers Association (CBA)[1] in response to the above referenced proposed changes to Regulations Z, B, E, M and DD, and the official staff commentaries under each of them (the "Proposal"), published by the Board of Governors of the Federal Reserve System (the "Board") on December 10, 2003. CBA appreciates the opportunity to share our comments.

The Proposal would revise the standard for "clear and conspicuous" disclosures as required by each of these regulations. In the case of Regulation Z, the Proposal also contains certain other revisions. Therefore, we have divided our comments into several parts: The first addresses the "clear and conspicuous" disclosures, and includes comments that apply to all five affected regulations. The second part is limited to the proposed amendments to the Regulation Z Commentary, and the third responds to the Board's request for information about debt cancellation agreements.

[1] The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

I. “Clear and Conspicuous” Standard

CBA strongly recommends that the Board withdraw the portion of this Proposal that would change the “clear and conspicuous” standard. We believe it would be an unwarranted change that would involve a significant cost to financial institutions, and ultimately to consumers, with no demonstrable improvement in disclosures.

The Board’s Proposal would take the new "clear and conspicuous" standard from Regulation P (where it applies to Privacy Notices) and use it for five other consumer disclosure rules (Regulations B, Z, M, E, and DD). Each of the regulations already has a slightly different variation on the same principle, that all disclosures should be clear and conspicuous. CBA has always supported clear and conspicuous disclosures of important consumer information. And, to our knowledge, there has never been a significant question about the meaning of the term as it is used in these regulations; even where it differs slightly (e.g. Regulation E), it has generally been regarded as the same in meaning.

As proposed, all the regulations would substitute the definition of “clear and conspicuous” found in Regulation P, which is that notices must be “reasonably understandable and designed to call attention to the nature and significance of the information.” They also list illustrations of what it means to be clear and conspicuous. Examples of a reasonably understandable disclosure include: “clear, concise sentences, paragraphs, and sections”; “short explanatory sentences or bullet lists”; “definite, concrete, everyday words"; and the avoidance of legal and highly technical business terminology.”

Examples of ways to call attention to the nature and significance of the information include the use of a plain-language heading; the use of easy-to-read type size (“Disclosures in 12-point type,” it says, “generally meet this standard”); wide margins and ample spacing; and boldface or italics for key words. When combining disclosures with other information, one should use “distinctive type size, style, and graphic devices, such as shading or sidebars.” While these examples are not mandatory, they would be evidence of clear and conspicuous disclosures.

<u>We believe that, while well-intentioned, these Proposals would do more harm than good, and would result in great cost to financial institutions. We respectfully request that the Board withdraw them.</u>

The problems with the proposal include the following:

<u>**The cost of this change would be enormous.**</u>

The proposal was presented as a technical change to these regulations with the suggestion that it would have a minimal compliance impact. According to the Initial Regulatory Flexibility Analysis that accompanied each of the proposals, “The proposed amendments are not expected to have any significant impact on small entities.” Similarly under the Paperwork Reduction Act review for state member banks that accompanied the proposals, the Board states, “While the proposal would amend Regulation Z and the staff commentary, it is expected that these revisions would not increase the paperwork burden of creditors.” The Board provides no supporting information to justify these conclusions.

We do not agree that this change is trivial. The concepts articulated in the Proposal represent a considerable recasting of the existing “clear and conspicuous” standard. In particular, the notion that disclosures must be “designed to call attention to the nature and significance of the information” introduces a new and entirely untested concept into the analysis. When an item is designed to call attention to the nature and significance of the information it contains, it must not merely be conspicuous, but arguably ***more*** conspicuous than other information in its vicinity. This is supported by the examples, which calls for various devices for making the disclosures “distinctive.” In a vacuum, the concept of disclosures that stand out from the surrounding information may have merit. However, in the real world, particularly where disclosures are integrated with contract terms and other state and federal disclosures, it would often result in a lengthier**,** less clear, and more confusing set of documents that would be of no benefit to the consumer. In some cases (for example, a typical motor vehicle lease), one might find a combined contract/disclosure document with the following information: Segregated Regulation M disclosures in a ‘federal box’; non-segregated Regulation M disclosures integrated with the contract terms and comprising fully half of the remaining document; several different state mandated disclosures with varying degrees of type-size or conspicuousness requirements; and the contract terms themselves.

To make matters more complicated, integrated disclosures are often set out in ways that make sense only within the context of the contract. If they had to be highlighted so as to call attention to their nature and significance, perhaps with a heading, the documents would need to be completely redesigned so all the disclosures would be organized to suit the regulation. There are many instances when it is not clear where a contract term ends and a required disclosure begins. There is no question that many forms would need to be longer simply because of the redundancy that would result. In effect, this would force many documents into a *de facto* “segregation” of disclosures from contract terms, notwithstanding the language of the regulations permitting integrated documents.

The language of the examples would in many cases place financial institutions in a position of having to adopt changes, even though they are not explicitly required. Avoiding liability risk is a desirable goal for institutions that wish to avoid unnecessary liability expense. If an official staff interpretation says that 12-point type always passes muster, while smaller type may be suspect, an institution will often choose the safer course, even at greater initial expense.

The impact—as a cost and a burden to financial institutions—promises to be huge by any standard of measure. The proposals would call for a review and possible rewrite of vast numbers of documents. Change in the long-standing, and well-understood disclosure requirements will force institutions to undertake a complete due-diligence review of affected documents and make appropriate changes to ensure compliance. A vast number of the retail forms in use today include some notice or disclosure mandated by at least one of the five affected regulations.

The re-examination of all the forms and the resulting changes, wherever necessary, will undoubtedly entail ***billions of dollars*** in compliance cost to the industry. When asked for an assessment of the potential cost of the Proposal, one banker estimated that it would cost her institution alone millions of dollars. She then said the following:

> We have many, many products within the bank as well as those of many lending affiliates, and if all the disclosures had to be revised, reviewed, approved by an outside attorney or even an in-house attorney, changing systems that now produce many of the disclosures, creating additional programming for our already overworked programmers, wasting of all disclosures and booklets that are printed that are not on the system, retraining our staff (which is huge) and tying up the Compliance Staff for probably a year to re-examine and see what needs changing, all this is very expensive especially in times when banks are struggling to make earnings. This seems very unnecessary if there has not been a huge amount of problems (that none of us know about). We are all for uniformity and consistency but in this case, just to be consistent with Regulation P is not worth having to do all of this.

Even if the review of these documents results in no significant changes—which we do not expect, as explained further below—the cost of the review would alone be enormous because of the shear volume and variety of documents involved. Not only would there be these transition costs, but there would be recurring incremental costs for paper, printing, and compliance review.

<u>The change would result in significant litigation expense</u>.

The Truth in Lending Simplification and Reform Act, more than two decades ago, was in major part an attempt to curtail the frivolous litigation that was becoming commonplace under that law. TILA's statutory damages provision permitted a consumer to sue a creditor for a minor technical violation of the Act and recover damages without proving actual damages. This encouraged litigation over the most trivial, technical matters, which had no significant impact on the consumer's credit decision. These individual actions, and the class actions that also proliferated, were widely recognized as a problem for creditors and, ultimately, for consumers of financial services.

Sadly, this proposed change in format rules will now result in a new round of litigation over hyper-technical matters, with all the cost and burden that will entail. The new requirements call for a subjective determination of whether disclosures are "reasonably understandable" and "designed to call attention to their nature and significance." Although the first concept (reasonably understandable) is not unlike the existing requirements, the requirement that disclosures be designed to call attention to their nature and significance will call for an entirely new analysis of what is compliant. Any compliance officer, any consumer, any examiner or any court may have an independent idea of what qualifies as fully in compliance. That is an open invitation for litigation.

Under Regulation P, a consumer has no private right of action for violations in compliance, so the problem is not as severe. But by extending this definition to five other consumer regulations, the Fed is subjecting the industry to considerable liability risk. Even if financial institutions win the majority of cases, the cost of litigating or settling would be very large.

The Board Presents No Evidence to Support the Need for this Change

A change of this significance calls for a substantial justification, buttressed by some significant evidence in support. ***The Board provides no such justification.*** Instead, the Supplementary Information provides two principal reasons for the action: First, the Board states that the "the recently implemented standard in Regulation P (65 FR 35162, June 1, 2000), articulates with greater precision than the other regulations the concepts underlying the duty to provide disclosures that consumers will notice and understand." Second, the Board states that the change will provide consistent guidance among Board regulations, and that "consistency among the regulations should facilitate compliance by financial institutions." Both statements stand unsupported and neither comes close to justifying the Proposal, with the considerable cost and burden that it entails.

The Regulation P standard, when adopted by the other regulations, does not articulate the concepts with greater precision; on the contrary, it creates enormous problems when applied to other regulations. The concept as applied to privacy notices, with the list of examples spelling out its application, may be clear and free from ambiguity in that context[2], but not so when applied to disclosures under Regulations Z, E, B, M and DD. Privacy notices are often provided in one format, with little variation based on individual circumstance and requiring little alteration. However, these other regulations require numerous different forms of disclosures that apply in many different situations for a huge number of financial products. The format requirements for each are

[2] Ironically, the agencies are now considering how they may improve the readability of the lengthy and complex privacy notices, given the concerns raised by industry and consumers. See Interagency Proposal to Consider Alternative Forms of Privacy Notices under the Gramm-Leach-Bliley Act. 68 FR 75,164 (Dec. 30, 2003). Thus, one wonders if the standard is the ideal suggested by the Proposal to adopt it across the board at this time.

unique, making the new concept challenging, if not impossible to satisfy with confidence in all of those settings.

Privacy notices are often sent as free-standing communications, unrelated to account activity. Consumers may have quite different perspectives on, and incentives to find and read, disclosures contained in periodic statements reviewing last month's account activity, or in credit card solicitations received in the mail, or in the extensive documentation and serial disclosures of mortgage transactions, or in ATM receipts hurriedly pocketed, or in a creditor's adverse action notice rejecting the consumer's application. Context is everything, and a monolithic rule on "clear and conspicuous" is not necessarily an improvement on the status quo.

In short, this change would call for a costly review and rewrite of every contract containing disclosures-- with no promise of better disclosure, and no guarantee that the final product could avoid liability under the new standard. For these reasons, we urge the Board to withdraw the proposals that would amend the "clear and conspicuous" requirement for Regulations Z, B, E, M and DD.

II. Other Regulation Z Commentary Proposals

<u>Clarification of "amount." [Commentary 2(b)-2].</u>

The staff would amend the Commentary to specify that any "amount" required to be disclosed must be stated as a numerical amount rather than in narrative form. CBA has no objection to this clarification, in the interest of consistency throughout Regulation Z. We would note, however, that a numerical amount (such as the amount of the monthly payment) would presumably need to be designated as an "estimate" if the monthly payment is derived from an amount financed that is itself an estimate. We believe this piling of estimates on estimates is not a desirable result as a general proposition.

<u>Rescission notice to creditor's agent [Commentary 15(a)(2)-1; 23(a)(2)-1]</u>.

The staff proposes that, where a creditor fails to furnish rescission forms or fails to designate an address to which the consumer might send the notice, the notice is effective when given to a third party (such as a servicer) if state law would consider that effective delivery to the actual creditor or assignee. We appreciate the need to protect the consumer's rescission rights where the place to send the rescission notice is not properly specified. We agree with the implication of the proposal that in any case notice to the actual creditor or its assignee is sufficient. But for other situations the interjection of a test based on state law agency principles (implied/apparent authority, estoppel, ratification, etc.) adds unnecessary complexity and uncertainty, and probably non-uniform resolutions of what is ultimately a TILA issue. It would be preferable, in our view, to specify that where an appropriate addressee is not identified in the rescission forms, the consumer's notice of rescission is effective if sent to the person to whom, or the address to which, payments are to be made under the agreement. This would of course include the creditor itself (or an assignee), but would also include a third-party servicer or even a mail drop address where that is the only guidance the consumer has.

Sequence of rescission procedures [Commentary 15(d)(4)-1; 23(d)(4)(1)].

The staff proposes language to clarify that a consumer's right to rescind "is not affected by" the procedures involving repayment of the credit or termination of the security interest. We concur with this objective as the staff describes it in the Supplementary Information, but question whether the proposed Commentary language is sufficiently precise and narrow. We do not understand that it is staff's intention to undercut a significant line of U.S. Court of Appeals holdings concerning the appropriate unwinding of rescindable transactions, nor to require creditors to terminate liens or refund payments before it is determined that the consumer is entitled to rescind. Rather, the intent is to prevent consumers from facing the dilemma of not being able to establish the right to rescind because of potential inability to repay or refinance the loan principal. If so, language drawn from the Supplementary Information would seem to make the point more clearly. *E.g.:*

> "The sequence of procedures under subsections (d)(2) and (d)(3), or a modification of them by a court, does not affect a consumer's ability to establish the substantive right to rescind and to have the lien amount adjusted accordingly."

III. Other information

a. Information regarding Debt Cancellation and Debt Suspension Agreements.

At this point CBA has received very little information about its members' use of Debt Cancellation Agreements (or Debt Suspension Agreements) outside of the boundaries of existing 226.4(d)(1) and 226.4(d)(3). Thus we cannot comment helpfully on the nature, or extent of use, of debt cancellation or suspension products tied to "life-cycle events" or the like. In general we continue to believe that the costs of genuinely optional products or services are not finance charges. But side agreements that become, in effect, default insurance may be another matter.

A foreseeable complication is that a creditor may offer, for a single fee, a combination package of DCA-type products, including some coverages within existing 226.4(d)(3)(ii), and some outside that subsection. This bundling of coverages would effectively be barred if the components of the DCA package were subject to different rules on disclosure or finance charge characterization. At least at the threshold, this suggests that variations on DCA coverage ought to be treated consistently with existing 226.4(d)(3).

On the matter of card issuers converting from credit insurance to DCA products, since they are treated so comparably in 226.4(d), we believe it should be sufficient for the card issuer to give the 226.9(f) notice without requiring a whole new disclosure and authorization for the DCA replacement product. If the OCC insists on requiring a separate consumer authorization in this context, perhaps the commentary to 226.9(f) could indicate that satisfaction of the OCC rule also satisfies 226.9(f).

b. Procedure for Information Gathering

We wholeheartedly support the Board staff's desire to obtain information from the public regarding issues for which the Staff perceives that there may be a need for future rulemaking. However, we believe that the current rulemaking Proposal is the incorrect vehicle and we would respectfully ask the staff not to use it for this purpose. A proposed rulemaking begins a formal administrative process with a timetable for comment and the prospect of a final change to the rule. When the Board staff wishes to gather comments prior to a rulemaking, the appropriate vehicle would be an Advance Notice of Proposed Rulemaking.

Using the correct vehicle puts the public on notice as to the nature of the process. By using the Supplementary Information accompanying a proposed rulemaking merely to gather information, the staff risks confusing the public into believing that a rulemaking process involving that information is farther advanced than it really is. At the same time, it runs the risk that the public will not be aware that the proposal is being used as an information gathering tool on a subject unrelated to the actual proposal. This is particularly true if, as here, the preamble in the Federal Register does not mention that the Proposal is also being used to gather unrelated information. So while some may comment out of an excessive concern that the issue is ripe for rulemaking, others may fail to comment because they are not aware that comment is being sought.[3]

Thank you for considering these comments.

Sincerely,

Steven Zeisel
Senior Counsel

Ralph Rohner
Special Counsel

[3] In this regard, it is worth noting 1 C.F.R. § 18.2 and 1 C.F.R.§18.12, relating to the preparation of documents for the Federal Register. The former section provides that "[t]he Director of the Federal Register will not accept a document for filing and publication if it combines material that must appear under more than one category in the Federal Register. For example, a document may not contain both rulemaking and notice of proposed rulemaking material." 1 C.F.R. § 18.2(a). The latter requires that, in preparing a notice of a proposed rule or an advance notice of proposed rulemaking for publication in the Federal Register, an agency provide a preamble that "will inform the reader, who is not an expert in the subject area, of the basis and purpose for the rule or proposal." 1 C.F.R. § 18.12(a).